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SUBJECT: PAKISTANI DELEGATION INFORMS U/S JEFFERY OF  
TALKS WITH IMF ON A FORMAL PROGRAM

Classified By: Under Secretary for Economic, Business and Agricultural Affairs, Reuben Jeffery for reasons 1.4 (b) and (d).

¶1. (C) Summary. In an October 11 meeting with U/S Jeffery, Pakistani Advisor to the Prime Minister on Finance and Economic Affairs Shaukat Tareen said that he is in talks with the International Monetary Fund (IMF) to reach an understanding on a formal Fund program before departing Washington, so that he can present a proposal to President Zardari. Key issues, he said, will be raising interest rates, borrowing from the central bank, and determining the size of the IMF package. Tareen and State Bank of Pakistan Governor Shamshad Akhtar stressed that in return for undertaking a politically unpopular Fund program that inflicts further pain on the Pakistani people, the GOP will need a large assistance package that shores up reserves, reestablishes creditworthiness, and focuses on the medium-term balance of payments scenario. If Georgia received five times its IMF quota, Pakistan -- in the middle of a war -- needs six times its quota, or about USD 9 billion. (Note: when U/S Jeffery met with IMF staff on October 8, IMF Director Mohsin Khan referred to possible exceptional access of USD 2 billion, with perhaps USD 1 billion front loaded.) The GOP seeks USG help vis-a-vis the IMF. To sell the package domestically, the GOP will say that the IMF has endorsed Pakistan's own reform plan. Tareen confirmed his strong, personal commitment to the Reconstruction Opportunity Zones (ROZs) and quick conclusion of a Bilateral Investment Treaty (BIT). Finally, the GOP made a quick pitch for early release of Coalition Support Funds, noting that at the September 29 Strategic Dialogue, the U.S. had promised to look at new procedures within two weeks. End Summary.

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GOP's Introductory Comments on the Economy

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¶2. (C) Tareen emphasized that the GOP's economic measures have caused considerable financial pain for Pakistanis, especially the elimination of some 550-600 billion rupees in subsidies over the last 6 months. On the overall economy, Tareen noted that FDI has slowed and the GOP has been unable to carry out privatizations in the current market environment. The GOP plans to reduce the fiscal deficit from 7.4 percent of GDP to 4.2 - 4.3 percent; streamline the revenue department in an effort to raise revenue collection from 10.5-11 percent to 15 percent of GDP; improve the social safety net by providing skilled training to one person per household in the poorest 30 percent of total households; increase competitiveness of manufacturing; encourage public-private partnerships; emphasize poverty alleviation programs; and develop

capital markets.

Pakistan Seeks USD 9 Billion Formal IMF Program

¶3. (C) Tareen stated that GOP reforms to date were addressing the external trade imbalance, fiscal deficit and social sectors (e.g. through major subsidy cuts and increases in electricity tariffs). The main problem now is the current account: foreign direct investment into Pakistan is slowing, and the GOP cannot proceed with privatization in the current climate. In addition, S&P and Moody's have cut Pakistan's ratings. Although the USG and others had formed the "Friends of Pakistan" group, assistance flows and the Saudi oil facility had not materialized. Low GOP reserves (covering only one to two months of imports) were feeding market nervousness; newspapers were reporting that Pakistan will default in January. The ADB has provided \$500 million and the GOP is hearing that \$600 million from the World Bank and other assistance flows will depend on having a formal IMF program.

¶4. (C) Tareen said that, although Pakistan has done all but "a couple" of things, the IMF was not going to endorse the GOP's home-grown program, and was instead asking the GOP to sign on to a formal Fund program. Tareen is talking to the IMF, but noted the GOP has already taken strong measures. Having inflicted pain on Pakistan's people, it would be difficult to tell the people that more pain will follow. Tareen would meet with the IMF over the weekend (including a meeting with Managing Director Strauss-Kahn on the afternoon of October 12) with the aim of reaching an understanding with the IMF before departing Washington so that he can present it to President Zardari. Raising interest rates and central bank borrowing would be key points. The GOP would have to gain "maximum mileage" from the IMF, however. If Georgia had obtained five times its IMF quota, Tareen argued that Pakistan, in the middle of a war, should get more.

¶5. (C) U/S Jeffery said he was gratified to hear Tareen's intention to seek an IMF program, and understood that the GOP would face domestic political problems. Two weeks ago, USG advice had been to get an IMF program or, at a minimum, IMF monitoring. Given the situation in international financial markets, the GOP could make the case that it was taking steps to protect Pakistan's economy. The IMF's work will pick up pace and U/S Jeffery urged the Pakistanis to sign up early. While U/S Jeffery could not comment on how difficult the negotiations might be, he stressed that the IMF cares deeply about Pakistan and is prepared to move swiftly, with quick-disbursing assistance that will in turn enable Pakistan to obtain help from the World Bank and donor community.

¶6. (C) Tareen understood that the IMF can put Pakistan on a fast track and move within two weeks, but sought USG help vis-a-vis (exact words: "sitting on") the Fund. Given the difficulty of selling a Fund program to the public, Tareen returned to the idea that, if Georgia obtained five times its IMF quota allocation, Pakistan would need six times its quota -- or roughly \$9 billion, which would stabilize the situation for 15 months or so. State Bank of Pakistan Governor Akhtar emphasized Pakistan's need for a large IMF package that maximizes GOP leverage. Pakistan needs to build reserves (to cover three months of imports) and restore creditworthiness, with a view toward the medium-term balance of payments scenario. Both on economic and domestic political grounds, the GOP needs to leverage its IMF quota as much as possible; a small IMF package will not achieve Pakistan's goals.

¶7. (C) U/S Jeffery stated that the IMF was aware of Pakistan's sacrifices to date. Director Mohsin Khan had said that the GOP had taken the most difficult steps already, i.e., cutting fuel subsidies. U/S Jeffery emphasized the need for quick action. Tareen stressed that, given current economic circumstances, the conflict with the Taliban, and increasing poverty, the GOP does not want to default. According to Tareen, the IMF Deputy Managing Director told him that Pakistan would need to do "very few" things. To sell the package domestically, the GOP would say that the IMF endorsed the GOP's plan. Pakistan's experience with the IMF in the 1990's had not been salutary. Tareen restated his intention to return to Pakistan with a proposal for presentation to Zardari. Tareen wants to proceed quickly; he understands that there is little time. The size of the package would be the key element.

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ROZs and BIT  
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¶8. (C) Tareen expressed appreciation for USG generosity and assistance, and noted the importance of proceeding with the Reconstruction Opportunity Zones (ROZs). He suggested that more thought be given to ROZ locations, specifically where in the FATA, in creating opportunities for economic prosperity. A/S Sullivan emphasized active U.S. efforts to pass current legislation; perhaps at a later point, both sides could examine possible expansion of product coverage and geographical areas. A/S Sullivan raised the bilateral investment treaty; both sides are looking at dates. Tareen stated that, even if it required his personal participation in the meetings, he wanted to get the BIT done - and quickly.

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